

## **EXHIBIT 1**

### **INTRODUCTION**

The California Department of Water Resources (“DWR”) is a state agency. DWR’s purpose is to provide dam safety and flood control services, and operate and maintain the State Water Project, which is the largest, state-run, multiple use water and power system in the nation.

In February 2001, in response to a state of emergency and executive order issued by Governor Gray Davis, DWR promptly created the California Energy Resources Scheduling division (the “CERS division”). Over the next several months, from January 2001 to May 2001, DWR contracted with various individuals and companies to staff the new CERS division with dozens of consultants.

As required by the Political Reform Act (the “Act”)<sup>1</sup> and DWR’s conflict of interest code, each consultant was required to file a statement of economic interests within 30 days of assuming office. On the statement, each consultant was required to disclose his or her investments and interests in real property held on the date of assuming office, and income received during the previous 12 month period. In this matter, 52 consultants did not timely file an assuming office statement of economic interests. As the filing officer for the consultants’ statements of economic interests, DWR was required by the Act to determine whether the required documents were timely filed, and if not, promptly notify the consultants of their obligation to file. DWR failed to do so, in violation of Section 81010.

For the purposes of this Stipulation, Respondent’s violations are stated as follows:

### **COUNTS 1-52**

On or about and between February 25, 2001 and January 9, 2002, Respondent California Department of Water Resources failed to determine whether 52 consultants timely filed their assuming office statements of economic interests, and if not, promptly notify the consultants of their obligation to file, in violation of Section 81010.

### **SUMMARY OF THE LAW**

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<sup>1</sup> The Political Reform Act is contained in Government Code sections 81000 through 91014. All statutory references are to the Government Code unless otherwise indicated. The regulations of the Fair Political Practices Commission are contained in sections 18109 through 18997 of Title 2 of the California Code of Regulations. All regulatory references are to Title 2, Division 6 of the California Code of Regulations, unless otherwise indicated.

## **Conflict of Interest Code Requirements**

An express purpose of the Act, as set forth in Section 81002, subdivision (c), is to ensure that the assets and income of public officials, which may be materially affected by their official actions, be disclosed, so that conflicts of interest may be avoided. In furtherance of this purpose, Section 87300 requires every agency to adopt and promulgate a conflict of interest code. The agency's conflict of interest code must specifically designate the employees and contractors of the agency who are required to file statements of economic interests disclosing their reportable investments, business positions, interests in real property, and other income.

Under Section 82019, subdivision (c), and Section 87302, subdivision (a), the persons who must be designated in an agency's conflict of interest code are the officers, employees, members, and consultants of the agency, whose position entails making, or participating in making, governmental decisions that may have a reasonably foreseeable material effect on any economic interest.

As mandated by Section 87302, subdivision (b), an agency's conflict of interest code must require a new consultant to file a statement of economic interests within thirty (30) days of assuming office. On the statement of economic interests, the consultant must disclose his or her investments and interests in real property held on the date of assuming office, and income received during the 12 months before assuming office. Section 87300 provides that a conflict of interest code has the force and effect of law, and any violation of the code is deemed a violation of the Act.

### **Definition of "Consultant"**

Regulation 18701, subdivision (a)(2) defines a "consultant," for the purposes of Section 82019, as an individual who, pursuant to a contract, makes specified governmental decisions, or serves in a staff capacity with the agency and in that capacity participates in making specified governmental decisions. Under Regulation 18702.1, an individual contractor of a governmental agency "makes a governmental decision" when the contractor, among other things, commits the agency to any course of action, or enters into any contractual agreement on behalf of the agency. Under Regulation 18702.2, the contractor "participates in making a governmental decision" when the contractor negotiates with third parties, or advises or makes recommendations to the agency's decision makers, without significant intervening substantive review.

### **Duties of Filing Officers**

The filing officer for statements of economic interests is the person or agency, which receives and retains original statements of economic interests. (Section 82027 and Regulation 18115.) Under Section 87500, subdivision (o), the filing officer for statements of economic interests filed by a consultant is the state agency that has contracted with the consultant. Section 81010 sets forth the duties of filing officers, and requires filing officers to: (1) supply the necessary forms and manuals prescribed by the Commission; (2) determine whether required documents

have been filed, and, if so, whether they conform on their face with the requirements of the Act; (3) notify promptly all persons who have failed to file a statement in the form and at the time required by the Act; and (4) report apparent violations of the Act to the appropriate agencies.

## SUMMARY OF THE FACTS

In February 2001, in response to a state of emergency and executive order issued by Governor Gray Davis, DWR created the CERS division to mitigate the effects of the energy crisis. Over several months, DWR contracted with various individuals and companies to staff the new CERS division with dozens of consultants.

As mandated by DWR's conflict of interest code, each consultant had a duty to file a statement of economic interests ("SEI") within 30 days of assuming office. On the SEI, each consultant was required to disclose his or her reportable investments and interests in real property held on the date of assuming office, and income received during the previous 12-month period. DWR's conflict of interest code applied the broadest disclosure requirements to consultants. However, if a consultant's duties were limited in scope, the Director of DWR had the authority to modify his or her disclosure category.

Notwithstanding DWR's conflict of interest code, 52 consultants did not timely file an assuming office SEI within 30 days of assuming office. When the consultants failed to file an assuming office SEI, DWR had a duty to determine whether the required documents were filed, and if not, promptly notify the consultants of their obligation. DWR failed to perform these duties promptly, in violation of Section 81010.

According to initial determinations made by DWR, the 52 consultants who did not file their SEI within 30 days of assuming office fell into three categories: spot market traders, energy contract negotiators, and energy market or financial advisors.

**Spot Market Traders.** The spot market traders were individual consultants who entered into personal service contracts with DWR, for a term of six months, to work as traders and trading managers. These individuals purchased and sold electric energy on the "real time," "hour ahead," and "day ahead" markets operated by the Independent System Operator. These individuals had independent authority to bind DWR financially.

**Energy Contract Negotiators.** The energy contract negotiators were owners or employees of companies that were under contract with DWR. These companies included the Electric Power Group, Navigant Consulting, and Interstate Gas Company. Consultants from these firms engaged in direct negotiations with electric energy generators and marketers to obtain short and long-term energy supply contracts for the State. The individual negotiators made recommendations to CERS regarding the terms of these transactions. In some cases, CERS relied on the expertise of the negotiators when acting upon their recommendations. The negotiators had authority to indicate to trading parties when it appeared an agreement in principle had been

reached, but did not have signature authority to bind DWR financially.

**Energy Market and Financial Advisors.** The energy market and financial advisors were owners or employees of the firms, Deloitte & Touche; Montague DeRose and Associates; Orrick, Herrington & Sutcliffe; and Hardy Engineering; which were under contract with DWR. Consultants from these firms attended policy meetings, prepared reports, and gave advice on various policy issues. In some cases, CERS relied on the expertise of these advisors when making decisions on energy supply contracts.

The following table, organized according to the counts set forth in the exhibit, lists the following information: (1) the dates that each of the 52 consultants assumed office; (2) the job description of each consultant; (3) the employer of each consultant; (4) the dates that each of consultant filed their SEI; and (4) the number of days the SEI was overdue.

| <b>Job Description</b>           | <b>Counts/Consultant</b> | <b>Employer</b>          | <b>Start Date (2001)</b> | <b>File Date (2001)</b> | <b># Days Late</b> |
|----------------------------------|--------------------------|--------------------------|--------------------------|-------------------------|--------------------|
| Spot Market Traders (16)         | 1. Terry Sack            | CERS (personal contract) | Jan. 29                  | Jul. 12                 | 133                |
|                                  | 2. Michael Brown         | CERS (personal contract) | Jan. 29                  | Jul. 12                 | 133                |
|                                  | 3. William Mead          | CERS (personal contract) | Feb. 13                  | Jul. 12                 | 119                |
|                                  | 4. Arthur Primm          | CERS (personal contract) | Feb. 13                  | Jul. 12                 | 119                |
|                                  | 5. Elaine Griffin        | CERS (personal contract) | Feb. 20                  | Jul. 11                 | 111                |
|                                  | 6. Constantine Louie     | CERS (personal contract) | Feb. 20                  | Jul. 12                 | 112                |
|                                  | 7. Kelly Park            | CERS (personal contract) | Feb. 21                  | Jul. 12                 | 111                |
|                                  | 8. Isaac Tseng           | CERS (personal contract) | Feb. 26                  | Jul. 12                 | 106                |
|                                  | 9. An Nguyen             | CERS (personal contract) | Feb. 26                  | Jul. 12                 | 106                |
|                                  | 10. Bernard Barretto     | CERS (personal contract) | Mar. 1                   | Jul. 12                 | 102                |
|                                  | 11. Herman Leung         | CERS (personal contract) | Mar. 19                  | Jul. 12                 | 85                 |
|                                  | 12. Peggy Cheng          | CERS (personal contract) | Apr. 2                   | Jul. 12                 | 70                 |
|                                  | 13. Atsumi Ito           | CERS (personal contract) | Apr. 4                   | Jul. 12                 | 68                 |
|                                  | 14. Linda Ng             | CERS (personal contract) | Apr. 9                   | Jul. 12                 | 63                 |
|                                  | 15. Susan Lee            | CERS (personal contract) | Apr. 16                  | Jul. 12                 | 56                 |
|                                  | 16. Harry Cleveland      | CERS (personal contract) | May 20                   | Jul. 24                 | 36                 |
| Energy Contract Negotiators (23) | 17. Ronald Nichols       | Navigant Consulting      | Jan. 19                  | Jul. 16                 | 147                |
|                                  | 18. Catherine Elder      | Navigant Consulting      | Jan. 24                  | Jul. 24                 | 150                |
|                                  | 19. Vikram Budhraj       | Electric Power Group     | Jan. 25                  | Jul. 12                 | 137                |
|                                  | 20. James Dyer           | Electric Power Group     | Jan. 25                  | Jul. 12                 | 137                |
|                                  | 21. Richard Ferreira     | CERS (personal contract) | Jan. 31                  | Jul. 11                 | 130                |
|                                  | 22. Tom Skupnjak         | Navigant Consulting      | Feb. 1                   | Jul. 16                 | 134                |
|                                  | 23. Fred Mobasher        | Electric Power Group     | Feb. 1                   | Aug. 29                 | 173                |
|                                  | 24. M. Kabir Faal        | Navigant Consulting      | Feb. 1                   | Jan. 2, 2002            | 306                |
|                                  | 25. Jeffrey Van Horne    | Navigant Consulting      | Feb. 1                   | Jan. 2, 2002            | 306                |
|                                  | 26. Craig McDonald       | Navigant Consulting      | Feb. 5                   | Aug. 30                 | 178                |
|                                  | 27. David Swank          | Navigant Consulting      | Feb. 10                  | Sept. 6                 | 179                |
|                                  | 28. Timothy Haines       | Navigant Consulting      | Mar. 1                   | Jul. 13                 | 104                |
|                                  | 29. Tara Nolan           | Navigant Consulting      | Mar. 1                   | Jul. 12                 | 103                |
|                                  | 30. Sumner White         | Navigant Consulting      | Mar. 6                   | Jul. 16                 | 104                |

|                                    |                       |                          |         |              |     |
|------------------------------------|-----------------------|--------------------------|---------|--------------|-----|
|                                    | 31. Mark Skowronski   | Electric Power Group     | Mar. 7  | Jul. 24      | 109 |
|                                    | 32. Joe Judge         | Electric Power Group     | Mar. 19 | Jul. 16      | 89  |
|                                    | 33. Gregory Rowe      | Electric Power Group     | Mar. 19 | Jul. 16      | 89  |
|                                    | 34. Richard Germaine  | Navigant Consulting      | Apr. 10 | Jul. 26      | 76  |
|                                    | 35. Simon Freeman     | CERS (personal contract) | Apr. 16 | Jul. 10      | 54  |
|                                    | 36. Mark Baldwin      | Interstate Gas Co.       | May 15  | Jul. 24      | 40  |
|                                    | 37. Suzanne McFadden  | Interstate Gas Co.       | May 15  | Sept. 10     | 87  |
|                                    | 38. Joy Young         | Interstate Gas Co.       | May 15  | Sept. 10     | 87  |
|                                    | 39. Johnnie Painter   | Interstate Gas Co.       | May 28  | Sept. 10     | 64  |
|                                    | 40. Christian Dusel   | Navigant Consulting      | Jun. 4  | Jan. 2, 2002 | 181 |
|                                    | 41. Brett Franklin    | Navigant Consulting      | Oct. 8  | Jan. 9, 2002 | 93  |
| Market and Financial Advisors (11) | 42. Dominic Young     | Deloitte and Touche      | Jan. 21 | Jul. 12      | 140 |
|                                    | 43. James Bemis       | Montague, DeRose Assocs. | Jan. 25 | Jul. 12      | 136 |
|                                    | 44. Douglas Montague  | Montague, DeRose Assocs. | Jan. 25 | Jul. 12      | 136 |
|                                    | 45. Hamid Dayani      | Deloitte and Touche      | Jan. 29 | Sept. 6      | 189 |
|                                    | 46. Kendra Heinicke   | Deloitte and Touche      | Jan. 30 | Aug. 20      | 171 |
|                                    | 47. Darlene DeRose    | Montague, DeRose Assocs. | Feb. 1  | Jul. 12      | 130 |
|                                    | 48. Stanley Dirks     | Orrick, Herrington       | Feb. 1  | Aug. 28      | 180 |
|                                    | 49. Ronald Slater     | Montague, DeRose Assocs. | Mar. 1  | Jul. 12      | 103 |
|                                    | 50. Randall Hardy     | Hardy Engineering        | Mar. 6  | Aug. 31      | 147 |
|                                    | 51. Kimberly Stephens | Deloitte and Touche      | Mar. 23 | Jul. 12      | 79  |
|                                    | 52. William Green     | CERS (personal contract) | Apr. 16 | Jul. 16      | 60  |

DWR hired each of the 52 consultants over a period of ten months. In January 2001, within two weeks after the Governor issued his executive order, 12 energy consultants joined DWR to work on the energy crisis. The following month, in February 2001, 15 more energy consultants joined DWR. In March 2001, another 11 consultants joined DWR to work on the energy crisis.

Approximately six weeks after contracting with the first consultant, on or about March 1, 2001, CERS Deputy Director Raymond Hart approached DWR's Chief Counsel, Susan Weber, about whether any conflict of interest laws applied to energy contractors. No decision was made regarding that issue. Two weeks later, on March 16, 2001, Mark Gladstone of the San Jose Mercury News contacted DWR, and inquired whether energy consultant Vikram Budhraj, president of Electric Power Group, was required to file an assuming office SEI. Neil Gould, a staff attorney for DWR, informed the reporter that DWR had not yet made a determination on that issue.

Thereafter, DWR staff, both legal and program staff, spent the next two months, from March 16 to May 24, 2001, investigating the facts and conducting legal research on whether the energy contractors were required to file assuming office SEI's. First, the duties and activities of the consultants had to be evaluated in a manner that corresponded to the legal definition of "consultant." This evaluation focused on the meaning of the term "consultant," as defined by the Act, and as used in DWR's conflict of interest code, and on whether a broad or narrow disclosure category should apply to each of the consultants. Because of the demands on the agency and their

own lack of familiarity with the energy industry, the staff's research was complex and time-consuming. At the same time, they were responsible for reviewing Public Records Act requests, and responding to Public Records Act litigation.

In April 2001, another seven energy consultants joined DWR to work on the energy crisis in the CERS division. The following month, in May 2001, five more energy consultants joined DWR. On May 24, 2001, DWR staff submitted a memorandum to DWR Director Thomas Hannigan, Raymond Hart, and Chief Personnel Officer Gregory Rowsey. The memorandum listed those consultants who were required to file SEI's, and their newly defined disclosure categories. Raymond Hart signed the memorandum on May 30, 2001. Thomas Hannigan signed the memorandum on June 5, 2001.

In June 2001, three more energy consultants joined DWR. On June 15, 2001, Gregory Rowsey sent a memorandum to 27 consultants, advising them to file an assuming office SEI by July 16, 2001. Twenty-five of the 27 consultants complied with Mr. Rowsey's request, and filed an assuming office SEI before July 16, 2001. Two of the consultants were later deemed not to have filing obligations. Nine additional consultants also filed by July 16, 2001. On July 19, 2001, Mr. Rowsey sent another memorandum to an unspecified number of consultants, advising them to file an assuming office SEI. Six of the consultants filed an assuming office SEI the following week. Thereafter, DWR officials continued to review whether any other energy contractors had an obligation to file an assuming office SEI. Four consultants filed their SEI in August 2001; five consultants filed their SEI in September 2001; and four consultants filed their SEI in January 2002.

By taking several months to inform 52 consultants of their duty to file an assuming office SEI, DWR failed to promptly notify them of their obligation to file, in violation of Section 81010. DWR's violation led to 52 consultants making, and participating in making, governmental decisions that involved the purchase of millions of dollars of energy, for several months, without the public having the ability to monitor their activities for conflicts of interests.

In aggravation, before the energy crisis and the formation of the new CERS division, DWR had no procedures in place to ensure that consultants who worked for DWR complied with the disclosure provisions of DWR's conflict of interest code.

In mitigation, DWR was responding to a state of emergency. On January 19, 2001, Governor Gray Davis declared a state of emergency, and issued an executive order directing DWR to take steps necessary to respond to an energy crisis. Increases in the price of electricity had resulted in shortages of electricity, and affected California's economy, as well as the solvency of major public utilities. Blackouts occurring throughout California caused some business to experience economic losses, and affected services provided by law enforcement agencies, hospitals and schools.

In February 2001, in response to the executive order, DWR promptly created the CERS division. Within a few days, DWR changed from a state agency charged with administering the state's water assets to one with the responsibility of meeting the state's electricity demands.

DWR's previous experience with providing electricity was limited to buying and selling power for the state water project. The state water project had a peak demand of 2,400 megawatts. During the energy crisis, the new CERS division handled a peak demand of 17,000 megawatts. DWR did not have a sufficient number of qualified staff members to perform its new duties. Upon its creation, the new division had more than 90 staff vacancies. DWR was not able to hire enough new state employees fast enough to fill those vacancies.

DWR's primary concern was obtaining enough energy to prevent future blackouts. During the time the violations occurred, many DWR employees and consultants worked 60 to 80 hours per week. In addition to handling the energy crisis, DWR staff spent a significant amount of time and resources responding to public requests for agency documents, including energy contracts, under the Public Records Act.

DWR eventually complied with its obligation as filing officer by determining that 52 contractors qualified as consultants, and advising them to file their SEI's. To avoid violations in the future, DWR has adopted new procedures to incorporate consultants into the SEI notification process used for DWR employees.

## **CONCLUSION**

This matter involves 52 violations of Section 81010 of the Act, and carries a maximum administrative penalty of Five Thousand Dollars (\$5,000) per count, for a total administrative penalty of Two Hundred and Sixty Thousand Dollars (\$260,000).

However, the emergency circumstances under which these violations occurred justify a penalty less than the maximum penalty. In fashioning a resolution, the Enforcement Division took into account the specific duties of the three types of consultants that were involved, and the length of time that their SEI filings were overdue. Therefore, as the duties of spot market traders involved more than making mere recommendations, DWR's failure to promptly notify these types of consultants of their filing obligation justifies the imposition of a higher penalty for those counts. In addition, significantly late SEI's also justifies the imposition of a higher penalty for those counts where consultants filed more than 100 days late. Accordingly, penalties were assessed as follows:

### **COUNTS 1-10**

#### **Spot Market Traders Who Filed More Than 100 Days Late**

Spot market traders made governmental decisions involving energy contracts without disclosing to the public their relevant economic interests. Ten of the spot market traders filed their SEI's more than 100 days past the filing due date. DWR's failure to ensure that these 10 individuals timely filed their SEI's resulted in serious public harm. For a significant length of time, DWR's violations deprived the public of the ability to monitor whether these decision-makers had conflicts of interest. This type of violation might therefore call for a maximum administrative penalty of \$5,000. However, as the violations occurred in the context of the emergency crisis, the

administrative penalty of \$3,000 for each violation, for a total of \$30,000, is appropriate.

COUNTS 11-16

**Spot Market Traders Who Filed Between 60 and 90 Days Late**

Six of the 16 spot market traders filed their SEI's between 30 to 90 days past the filing due date. DWR's failure to ensure that these six individuals timely filed their SEI's resulted in serious public harm. However, as these individuals filed within 30 to 90 days of the filing due date, a penalty less than \$3,000 for each count is appropriate. Therefore, these counts justify an administrative penalty of \$1,500 per violation, for a total of \$9,000.

COUNTS 17-31, 40, 42-50

**Negotiators and Advisors Who Filed More Than 100 Days Late**

Negotiators and advisors made recommendations regarding energy contracts without disclosing their relevant economic interests. Unlike spot market traders, negotiators and advisors did not make governmental decisions, but only participated in those decisions by providing advice. As such, the resulting public harm was significant, but less serious than for spot market traders. Twenty-five of these 36 experts filed their SEI's more than 100 days after the filing due date. For a significant length of time, DWR's violations deprived the public of the ability to monitor whether these expert advisors had conflicts of interests. Accordingly, the appropriate administrative penalty for these counts is \$1,000 per violation, for a total of \$25,000.

COUNTS 32-39, 41, 51-52

**Negotiators and Advisors Who Filed Between 30 and 90 Days Late**

Eleven of the 36 energy experts filed their SEI's between 30 to 90 days past the filing due date. DWR's failure to ensure that these 11 individuals timely filed their statements of economic interests resulted in significant public harm. However, as these individuals filed within 30 to 90 days of the filing due date, a penalty less than \$1,000 for each count is appropriate. Therefore, these counts justify an administrative penalty of \$500 per violation, for a total of \$5,500.

Based on the foregoing facts and circumstances, a total administrative penalty of \$69,500 is justified.